2014

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Richard C. Ausness
University of Kentucky College of Law, rausness@uky.edu

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QUINNIPIAC PROBATE
LAW JOURNAL

VOLUME 27 2014 NUMBER 3

WHEN IS A TRUST PROTECTOR A FIDUCIARY?

RICHARD C. AUSNESS*

The use of trust protectors has become increasingly popular in the past twenty years. This is largely due to the fact that settlors can use trust protectors to provide more flexibility in trust management, especially for long-term trusts. However, the use of trust protectors is not without some risk.[1] First of all, the legal status of trust protectors is not explicitly recognized in some states. Furthermore, even in those states which do recognize the legality of trust protectors, the nature and extent of their powers is sometimes not always clear. Finally, there is the vexing question of whether trust protectors owe any fiduciary duties, and if so, what the nature of these fiduciary duties may be. In this Article, I will address a number of issues relating to the fiduciary duties of trust protectors.

Part I will briefly discuss the origins and legal status of trust protectors in the United States. Part II will examine the fiduciary duties of trustees and trust advisors in order to determine whether any of the fiduciary obligations imposed by law on other trust officers may be applied to trust protectors as well. In addition, Part II will consider statutes and case law on the subject in both foreign and American jurisdictions. Part III will explore the question of fiduciary duties in more depth and will conclude that the law should impose

* Everett H. Metcalf, Jr. Professor of Law, University of Kentucky; B.A. 1966, J.D. 1968 University of Florida; LL.M. 1973 Yale University. The author would like to thank Professor Franklin Runge, Faculty Services Librarian, for his help in obtaining foreign statutes and cases for use in this Article. In addition, the author relied on some of the material in Kathleen R. Sherby & Justin T. Flach, *Trust Protectors: The Role and Characteristics of a Third Party Decision Maker* (powerpoint presentation), TSUB03 ALI-ABA 1, 4 (July 26, 2012).

[1] *See* John H. Martin, *The Dynasty Trust in Ohio: A Short, Rigid, or Uncertain Reign*, 43 U. TOL. L. REV. 53, 57 (2011).

certain fiduciary duties on trust protectors, such as the duties of good faith, loyalty, impartiality, and independence. At the same time, it concludes that settlors should be given the power to modify these duties through appropriate language in the trust instrument. Finally, Part IV will suggest several drafting solutions that may reduce some of the uncertainty about the nature of a trust protector's fiduciary responsibilities.

I. TRUST PROTECTORS

A. Origins of the Office of Trust Protector

The modern office of trust protector can trace its origins back to a number of sources. These include: (1) non-trustee functionaries in England and in a number of Commonwealth countries; (2) similar individuals and financial institutions associated with offshore and domestic asset protection trusts; and (3) certain individuals known as trust advisors in America. For example, in England, trust protectors have been used in one form or another for many years.[2] Trust protectors are also recognized in a number of Commonwealth countries, particularly in the Caribbean region. Indeed, as early as 1893, the Bahamas Trustee Act permitted a settlor, to grant to a person who was not a trustee, the power to influence the actions of a trustee.[3] In recent years, other jurisdictions have enacted similar legislation.

However, the term "protector" was first employed in 1989 when the Cook Islands International Trusts Amendment Act expressly provided for trust "protectors."[4] The statute described the protector as "the holder of a power which whom invoked is capable of directing the trustee in matters relating to the trust and in respect of which matters the trustee has discretion and includes a person who is the holder of a power of appointment or dismissal of trustees."[5] Other Commonwealth jurisdictions subsequently adopted a more expansive view of the role of the trust protector. For example, the Belize Trusts Act provides that, in addition to the power to remove and replace a trustee[6], a trust protector may exercise any power "conferred on the

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[2] *See* Stewart E. Sterk, *Trust Protectors, Agency Costs, and Fiduciary Duty*, 27 CARDOZO L. REV. 2761, 2764 (2006).

[3] *See generally* BAHAMAS TRUSTEE ACT § 81 (1893).

[4] Richard Lewis, Note, *The Foreign Irrevocable Life Insurance Trust as Asset Protection: Potential for Abuse and Suggestions for Reform*, 9 CONN. INS. L.J. 613, 618 (2003).

[5] COOK ISLANDS INTERNATIONAL TRUSTS AMENDMENT 1989 § 3(2) (1989), *available at* http://www.paclii.org/ck/legis/num_act/itaa1989351/index.html.

[6] BELIZE TRUSTS ACT, ch. 202, § 16(2)(a) (2000 rev. ed.), *available at* http://www.lawyers-abogados.net/en/Resources/Belize/belize-trusts-act.pdf.

protector by the terms of the trust."[7] Similarly, the laws of both Anguilla[8] and Nevis[9] authorize the settlor to confer additional powers on the trust protector. Finally, in the British Virgin Islands, the Trust Ordinance of 1961 set forth a specific list of powers that may be conferred on a trust protector.[10] This provision authorizes a trust protector to determine the governing law of the trust, change the *situs* of the trust, remove trustees, appoint new or additional trustees, add or exclude trust beneficiaries, or withhold consent to actions of the trustees.[11]

The recent surge in the popularity of trust protectors in the United States is largely due to the use of trust protectors in connection with offshore asset protection trusts.[12] An asset protection trust is a self-settled spendthrift trust that is created to insulate the settlor's property from the claims of creditors.[13] Until recently, almost all American courts held that it was against public policy to allow settlors to thwart their creditors by making themselves the beneficiaries of a self-settled spendthrift trust.[14] For this reason, beginning in the 1980s, many U.S. citizens established self-settled spendthrift trusts, euphemistically referred to as "asset protection trusts" by practitioners, in foreign countries in order to take advantage of their debtor-friendly laws.[15] For example, many foreign jurisdictions made life difficult for mainland creditors by refusing to recognize orders and judgments from American courts and by enacting very short statutes of limitation for bringing fraudulent conveyance claims.[16] Although laws of this sort attracted their share of swindlers and deadbeats, they also encouraged many honest professionals, such as physicians, lawyers, accountants, and

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[7] *Id.* § 16(2)(b).

[8] ANGUILLA TRUSTS ACT, ch T70, § 15(2)(c) (2000 rev. ed.), *available at* http://www.fsc.org.ai/PDF/Insurance%20Act.pdf.

[9] NEVIS INTERNATIONAL EXEMPT TRUST ORDINANCE § 9(2) (1994), *available at* http://www.inttrust.com/Trust_Ordinance.pdf.

[10] *See* B.V.I. TRUSTEE ORDINANCE § 86(2) (1961) (amended 2003).

[11] *Id.*

[12] *See* Sterk, *supra* note 2.

[13] *See* Ritchie W. Taylor, *Domestic Asset Protection Trusts: The "Estate Planning Tool of the Decade" or a Charlatan?*, 13 BYU J. PUB. L. 163, 164 (1998).

[14] *See* Karen E. Boxx, *Gray's Ghost—A Conversation About the Offshore Trust*, 85 IOWA L. REV. 1195, 1202-03 (2000); *see also* Christopher M. Reimer, *The Undiscovered Country: Wyoming's Emergence as a Leading Trust Situs Jurisdiction*, 11 WYO. L. REV. 165, 168 (2011).

[15] Richard C. Ausness, *The Offshore Asset Protection Trust: A Prudent Financial Planning Device or the Last Refuge of a Scoundrel?*, 45 DUQ. L. REV. 147, 152 (2007).

[16] *See* James T. Lorenzetti, *The Offshore Trust: A Contemporary Asset Protection Scheme*, 102 COM. L.J. 138, 143-44 (1997); *see also* Taylor, *supra* note 13, at 169-75; *see also* Lewis, *supra* note 4, at 628.

engineers, to take advantage of the protection they afforded against American creditors by transferring their assets overseas.[17] Many of these professionals had legitimate concerns that large malpractice awards might wipe them out financially.[18]

In order to achieve the desired protection against domestic creditors, the settlor would designate a person or institution who was beyond the reach of American courts to serve as trustee of the asset protection trust.[19] However, Americans who set up these trusts were understandably reluctant to give up all control over their assets to a potentially unreliable foreign trustee.[20] Consequently, settlors were allowed to appoint trust protectors to safeguard their interests against possible wrongdoing by foreign trustees.[21] These trust protectors were typically given various powers over the trustee and the trust, including the power to make distributions from the trust, change the *situs* of the trust, and remove the trustee and appoint a successor trustee.[22] The settlor could also give the trust protector a "non-binding" letter of intent or letter of wishes to provide guidance to the trust protector about how the settlor wanted the trust property to be administered or distributed.[23]

In 1997, Alaska[24] and Delaware[25] became the first states to enact laws to authorize the creation of domestic asset protection trusts.[26] A number of other states quickly followed suit.[27] A domestic

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[17] Charles D. Fox IV & Michael J. Huft, *Asset Protection and Dynasty Trusts*, 37 REAL PROP. PROB. & TR. J. 287, 298 (2002).

[18] Elena Marty-Nelson, *Offshore Asset Protection Trusts: Having Your Cake and Eating It Too*, 47 RUTGERS L. REV. 11, 56-57 (1994).

[19] *See* Robert T. Danforth, *Rethinking the Law of Creditors' Rights in Trusts*, 53 HASTINGS L.J. 287, 309 (2002).

[20] Philip J. Ruce, *The Trustee and the Trust Protector: A Question of Fiduciary Power. Should a Trust Protector Be Held to a Fiduciary Standard?*, 59 DRAKE L. REV. 67, 76 (2010).

[21] *See* Donovan W. M. Waters, *The Protector: New Wine In Old Bottles?, in* TRENDS IN CONTEMPORARY TRUST LAW, 63-64 (A.J. Oakley ed., 1996).

[22] Ausness, *supra* note 15, at 155.

[23] *See* Denise C. Brown, *Caribbean Asset Protection Trust: Here Comes the Sun—Dispelling the Dark Clouds of Controversy*, 7 U. MIAMI BUS. L. REV. 133, 134 (1998).

[24] *See* ALASKA STAT. § 34.40.110 (2013); ALASKA STAT. §§ 13.36.035–13.36.60 (2013).

[25] *See* DEL. CODE ANN. tit. 12, §§ 3570-76 (2014).

[26] *See generally* Paul M. Roder, *American Asset Protection Trusts: Alaska and Delaware Move "Offshore" Trusts Onto the Mainland*, 49 SYRACUSE L. REV. 1253, 1267-74 (1999) (for a discussion of both Alaska and Delaware's statutes regarding domestic asset protection trusts).

[27] *See* Keith Adam Halpern, *Domestic Asset Protection Trusts: What Is Your State of Asset Protection?*, 7 FLA. ST. U. BUS. REV. 139, 140 (2008); Fox & Huft, *supra* note 17, at 320-38; Timothy Lee, *Alaska on the Asset Protection Trust Map: Not Far Enough for a Regulatory Advantage, But Too Far for Convenience?*, 29 ALASKA L. REV. 149, 168-71 (2012); *see generally* Richard W. Nenno, *Planning with Domestic Asset-Protection Trusts: Part II*, 40 REAL PROP. PROB. TR. J. 477 (2005).

asset protection trust is similar to an offshore asset protection trust, but avoids the complications and uncertainties associated with establishing a trust in a country that may have a foreign language and a different social culture, political system, legal system, and currency.[28] A number of these statutes provide for the appointment of trust protectors or trust advisors to protect the interests of the settlor.[29] These individuals may have the authority to remove trustees or veto any distributions from the trust.[30]

According to some commentators, the modern trust protector may simply be a version of the traditional office of trust advisor.[31] A trust advisor is a person who has power to exercise control over a trustee.[32] Traditionally, trust advisors supervised the trustee's investment decisions, but they have exercised broader powers as well.[33]

B. Current Legal Status of Trust Protectors

Although a majority of states now appear to recognize the legal status of trust protectors, at least implicitly, the legal landscape in this area is still sparse and uncertain.[34] For example, many of the statutes that purport to recognize the legitimacy of trust protectors say little about their powers, duties, or the potential status of trust protectors as fiduciaries.[35] Moreover, there is very little case law so practitioners in this area must exercise a considerable amount of caution.

At the present time, twenty-four states, including the District of Columbia, have adopted the Uniform Trust Code.[36] Section 808(c) of the Code permits a trust instrument to "confer upon a trustee or

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[28] Henry J. Lischer, Jr., *Domestic Asset Protection Trusts: Pallbearers to Liability?*, 35 REAL PROP. PROB. & TR. J. 479, 515-16 (2000).

[29] *See, e.g.*, ALASKA STAT. § 13.36.370(b)(1) (2013); DEL. CODE ANN. tit. 12, § 3570(8)(c)(1)–(3) (2011); UTAH CODE ANN. § 25-6-14(7)(b) (West 2013).

[30] *See, e.g.*, ALASKA STAT. §13.36.370(b)(1) (2013); DEL. CODE ANN. tit. 12, § 3570(8)(c)(1)–(3) (2011); UTAH CODE ANN. § 25-6-14(7)(b) (West 2013).

[31] *See* Alexander A. Bove, Jr., *The Case Against the Trust Protector*, 25 PROB. & PROP. 50, 51 (2011).

[32] Harvard Law Review Association, Note, *Trust Advisors*, 78 HARV. L. REV. 1230, 1230 (1965).

[33] *See* John P.C. Duncan & Anita M. Sarafa, *Achieve the Promise—and Limit the Risk—of Multi-Participant Trusts*, 36 ACTEC L.J. 769, 781 (2011); Ruce, *supra* note 20, at 75.

[34] *See* Duncan & Sarafa, *supra* note 33, at 789.

[35] *See id.* at 790.

[36] These include Alabama, Arizona, Arkansas, the District of Columbia, Florida, Kansas, Maine, Massachusetts, Michigan, Missouri, Nebraska, New Hampshire, New Mexico, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, South Carolina, Tennessee, Utah, Vermont, Virginia, West Virginia, and Wyoming. *See* JESSE DUKEMINIER & ROBERT H. SITKOFF, WILLS, TRUSTS, & ESTATES 389 (9th ed. 2013).

other person a power to direct the modification or termination of the trust."[37] In addition, a few state statutes provide a comprehensive list of the powers that trust protectors may legitimately exercise. For example, the South Dakota statute lists the following twelve powers that a trust protector may exercise if authorized by the trust instrument:

> (1) [m]odify or amend the trust instrument to achieve favorable tax status or respond to changes in the Internal Revenue Code, state law, or the rulings and regulations thereunder; (2) [i]ncrease or decrease the interests of any beneficiaries to the trust; (3) [m]odify the terms of any power of appointment granted by the trust [with the qualification that a modification or amendment may not grant a beneficial interest to any individual or class of individuals not specifically provided for under the trust instrument]; (4) [r]emove and appoint a trustee, a fiduciary provided for in the governing trust instrument, trust advisor, investment committee member, or distribution committee member; (5) [t]erminate the trust; (6) [v]eto or direct trust distributions; (7) [c]hange *situs* or governing law of the trust, or both; (8) [a]ppoint a successor trust protector; (9) [i]nterpret terms of the trust instrument at the request of the trustee; (10) [a]dvise the trustee on matters concerning a beneficiary; (11) [a]mend or modify the trust instrument to take advantage of laws governing restraints on alienation, distribution of trust property, or the administration of the trust; and (12) [p]rovide direction regarding notification of qualified beneficiaries pursuant to § 55-2-13.[38]

A Wyoming statute enables settlors to grant many of these same powers to trust protectors but adds some additional powers, including the power to: (1) "review and approve the accountings of a trustee" and (2) "elect for the trust to become a qualified spendthrift trust."[39] Of course, these enumerated powers are illustrative rather than exclusive so settlors may grant additional powers in the trust instrument.

An analysis of the various powers enumerated in these statutes suggests that a trust protector can play a number of roles in the administration of a trust. First, and foremost, the trust protector

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[37] UNIF. TRUST CODE § 808(c) (2000) (amended 2010).

[38] S.D. CODIFIED LAWS § 55-1B-6 (2013).

[39] WYO. STAT. ANN. § 4-10-710(a)(iv), (xii) (2009).

can oversee and supervise the activities of the trustee; second, he can advise the trustee on investment or other matters; third, he can act as mediator between the trustee and the trust beneficiaries; and fourth, he can perform certain functions that would ordinarily be performed by a court, such as modifying the terms of the trust instrument.[40] Of course, trust protectors will seldom exercise all of these powers, but in theory a trust protector could exercise most or even all of them if the trust instrument authorized him to do so.

II. AN OVERVIEW OF FIDUCIARY DUTIES

At common law, a fiduciary relation exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of the relation.[41] Fiduciary relationships typically impose some sort of fiduciary duties on one party. The nature of these fiduciary duties varies according to the underlying fiduciary relationship. However, the core principle involved is that one who owes a fiduciary duty to another must not put his or her interests ahead of the other but must act for the other's benefit.[42] Relationships that are deemed to be fiduciary in nature include: parent-child, attorney-client, doctor-patient, guardian-ward, and trustee-beneficiary.[43] Before considering the fiduciary duties that might be applicable to trust protectors, I shall examine the fiduciary duties that apply to other fiduciaries such as trustees and trust advisors.

A. Trustees

Two of the three most important duties of a trustee are loyalty and prudence in the conduct of trust administration.[44] There are also a number subsidiary duties, including the duty to collect and protect trust property, the duty to earmark trust property, the duty of impartiality, the duty not to mingle trust funds with the trustee's own property, the duty to inform and account, the duty to make trust property productive, and the duty not to delegate.[45]

The duty of loyalty has been called "the essence of the fiduciary relationship."[46] The Uniform Trust Code declares that "[a]

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[40] *See* Richard C. Ausness, *The Role of Trust Protectors in American Trust Law*, 45 REAL PROP. TR. & EST. L.J. 319, 329-33 (2010).

[41] RESTATEMENT (SECOND) OF TRUSTS § 2 cmt. b (1959).

[42] UNIF. TRUST CODE § 802 & cmt.

[43] Ruce, *supra* note 20, at 80.

[44] Louise Lark Hill, *Fiduciary Duties and Exculpatory Clauses: Clash of the Titans or Cozy Bedfellows?*, 45 U. MICH. J.L. REFORM 829, 832 (2012).

[45] *See generally* GEORGE T. BOGERT, TRUSTS §§ 97-101 (6th ed. 1987).

[46] J.C. SHEPHERD, THE LAW OF FIDUCIARIES 48 (1981).

trustee shall administer the trust solely in the interests of the beneficiaries."[47] This principle prohibits trustees from self-dealing or engaging in activities that constitute a conflict of interest.[48] Self-dealing includes the purchase of trust property by the trustee,[49] the sale of the trustee's property to the trust,[50] leasing of trust assets to the trustee,[51] or the trustee's borrowing of trust funds.[52] Under the so-called "no further inquiry" rule, a trustee cannot avoid liability for self-dealing by claiming to have acted in good faith.[53] In such cases, the self-dealing transaction is regarded as voidable and may be rescinded at the option of the beneficiaries.[54] The reason that self-dealing is prohibited is that the transaction is not an arm's length one because the trustee is both the buyer and the seller.

The duty of loyalty also requires a trustee to avoid a range of activities that might result in a conflict of interest.[55] For example, a trustee may not sell stock or other assets owned by the trust to a company where he is an officer or director,[56] sell trust property to a spouse or to close relatives,[57] or otherwise act in a way that is potentially contrary to the best interests of the beneficiaries.[58] Conflicts of interest can take many forms. An example of such a conflict is illustrated by In re *Mergenhagen*.[59] In that case, the beneficiaries of two irrevocable family trusts petitioned the surrogate

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[47] UNIF. TRUST CODE § 802(a); *see also* Mark S. Poker & Amy S. Kiiskila, *Prevention and Resolution of Trust and Estate Controversies*, 33 ACTEC J. 262, 266 (2008).

[48] John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 YALE L.J. 625, 655 (1995).

[49] *See* Home Fed. Sav. & Loan Ass'n of Chicago v. Zarkin, 432 N.E.2d 841, 846 (Ill. 1982); Presbyterian Church of Flemington v. Plainfield Trust Co., 52 A.2d 400, 401 (N.J. Ch. 1947); Marshall v. Carson, 38 N.J. Eq. 250, 256 (1884); Munsey v. Russell Bros., 213 S.W.2d 286, 289 (Tenn. Ct. App. 1948).

[50] *See generally* Marcellus v. First Trust & Dep. Co., 52 N.E.2d 907 (N.Y. 1943); *In re* Binder's Estate, 27 N.E.2d 939 (Ohio 1940).

[51] *See* Sherman v. Sherman, 751 N.W.2d 168, 173-74 (Neb. Ct. App. 2008); Anderton v. Patterson, 69 A.2d 87, 89 (Pa. 1949).

[52] *See In re* Estate of Stowell, 595 A.2d 1022, 1025 (Me. 1991); Veterans' Admin. v. Hudson's Estate, 179 A. 836, 838-39 (Md. 1935).

[53] *See* RESTATEMENT (THIRD) OF TRUSTS § 78 cmt. b (2007) (declaring that in cases of self-dealing, "it is immaterial that the trustee may be able to show that the action in question was taken in good faith, that the terms of the transaction were fair, and that no profit resulted to the trustee"); *see also* Fulton Nat'l Bank v. Tate, 363 F.2d 562, 571 (5th Cir. 1966).

[54] *See* Karen E. Boxx, *Too Many Tiaras: Conflicting Fiduciary Duties in the Family-Owned Business Context*, 49 HOUSTON L. REV. 233, 240-41 (2012).

[55] *See* Karen E. Boxx, *Of Punctilios and Paybacks: The Duty of Loyalty Under the Uniform Trust Code*, 67 MO. L. REV. 279, 282-83 (2002).

[56] *See In re* Estate of Martin, 86 Cal. Rptr. 2d 37, 41-42 (Ct. App. 1999); Tracy v. Cent. Trust Co., 192 A. 869, 870 (Pa. 1937).

[57] *See* UNIF. TRUST CODE § 802(c)(1)–(2) (2000) (amended 2010).

[58] *See In re* Trustees Under Yost's Will, 141 N.E.2d 176, 179 (Ohio Ct. App. 1956).

[59] *In re* Mergenhagen, 856 N.Y.S.2d 389 (App. Div. 2008).

court to remove David Mergenhagen as trustee.[60] When the surrogate court refused to do so, the petitioners appealed.[61] The appellate court ruled that the trustee should be removed, declaring:

> The loyalty of David Mergenhagen to his mother, the surviving grantor of the trusts, placed him in conflict with his duty as trustee, as evidenced by his administration of the trust for his mother's benefit despite the express language of the trust instrument prohibiting such conduct. In addition, his open hostility toward the other beneficiaries directly conflicts with his duty to the trust where, as here, that hostility has 'interfere[d] with the proper administration of the trust.'[62]

One of the most famous conflict of interest cases, In re *Rothko*, concerned a breach of the duty of loyalty by the executors of artist Mark Rothko's estate.[63] Rothko's estate consisted of almost 800 of his paintings.[64] In his will, Rothko directed his executors to sell the paintings and use the proceeds to fund the Mark Rothko Foundation, a charitable corporation.[65] Rothko named three of his friends—Bernard Reis, Theodoros Stamos, and Morton Levine—as executors and directors of the Foundation.[66] The executors agreed to sell Marlborough A.G. (MAG) 100 paintings for the exceedingly low sum of $1.8 million.[67] In addition, they consigned the remaining paintings to Marlborough Gallery, Inc. (MNY), to be sold over a twelve-year period at a fifty percent commission.[68]

Rothko's children brought suit against the executors and challenged the validity of the two contracts.[69] The court concluded that both Reis and Stamos had conflicts of interest and voided the contracts.[70] Reis was a director, secretary, and treasurer of MNY.[71] However, because Reis did not own MNY, he was not guilty of self-

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[60] *Id.* at 390.
[61] *Id.*
[62] *Id.* at 391 (quoting Matter of Rudin, 789 N.Y.S.2d 123, 124 (App. Div. 2005)).
[63] *In re* Rothko, 372 N.E.2d 291 (N.Y. 1977).
[64] *Id.* at 293.
[65] *Id.*
[66] *Id.*
[67] *Id.*
[68] *Rothko*, 372 N.E.2d at 293.
[69] *Id.* Although the children were not named as beneficiaries in Rothko's will, they were able to claim a share of his estate under New York's mortmain statute. *See* Boxx, *supra* note 55, at 288.
[70] *Rothko*, 372 N.E.2d at 296.
[71] *Id.* at 294.

dealing.[72] However, his involvement in negotiating the contracts between Rothko's estate and the two art galleries gave rise to a classic conflict of interest. In his role as executor, Reis was obligated to negotiate the best deal for the estate. However, as an officer of MNY, he was expected to obtain the best terms possible for his employer. In this case, the court found that Reis put the interests of his employer over those of the Rothko estate.[73]

The court found that Stamos also had a conflict of interest. According to the court, "it was to the advantage of coexecutor Stamos as a 'not-too-successful artist, financially,' to curry favor with Marlborough."[74] For this reason, the court concluded, Stamos agreed to the generous terms that Reis negotiated on behalf of the art galleries. In other words, like Reis, Stamos put his own interests ahead of the interests of the Rothko estate.[75]

The duty of prudence imposes an objective duty of care, similar to the reasonably prudent person standard of tort law, upon trustees with respect to the management and investment of trust property.[76] According to the Uniform Trust Code, this requires the trustee to "administer the trust as a prudent person would, by considering the purposes, terms, distributional requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution."[77] The duty of prudence arises most often in the area of the trustee's investment decisions. The principal standard for investing is known as the "prudent investor rule."[78] Section 2 of the Uniform Prudent Investor Act describes this rule as follows: "A trustee shall invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution."[79] Other jurisdictions have adopted a prudent person rule. This rule is not limited to investment decisions, but applies to other aspects of trust management as well.[80] According to this rule, a trustee may "make such investments . . . as a

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[72] *Id.* at 295-96.

[73] *Id.* at 296.

[74] *Rothko*, 372 N.E.2d at 294.

[75] *Id.* The court determined that Levine did not have a conflict of interest, but was nevertheless negligent in not objecting to the conduct of Reis and Stamos. *Id.*

[76] *See* Langbein, *supra* note 48, at 656.

[77] UNIF. TRUST CODE § 804 (2000) (amended 2010).

[78] *See* John H. Langbein, *The Uniform Prudent Investor Act and the Future of Trust Investing*, 81 IOWA L. REV. 641, 644 (1996).

[79] UNIF. PRUDENT INVESTOR ACT § 2(a) (1994).

[80] J. Alan Nelson, *The Prudent Person Rule: A Shield for the Professional Trustee*, 45 BAYLOR L. REV. 933, 936 (1993).

prudent man would make of his own property having in view the preservation of the estate and the amount and regularity of the income to be derived."[81]

The trustees in *Estate of Collins*[82] evidently failed to heed this dictum. Lamb, a business partner of the settlor, and Millikan, a lawyer, were named as the trustees of a testamentary trust established by Collins for the benefit of his widow, children, and parents.[83] However, the trustees lent most of the trust corpus to a construction company owned by two clients of Millikan.[84] The loan was secured by a second mortgage on certain property owned by the company.[85] The trustees did not inquire into the creditworthiness of the company, nor did they have the property appraised.[86] Had they done so, they would have discovered that the existing first mortgage exceeded the value of the property that secured the loan and that there were a number of foreclosures and lawsuits pending against the company.[87] A year later, the company and its owners declared bankruptcy and defaulted on the loan.[88] When the trustees sought to be discharged after having lost the entire trust corpus, the beneficiaries objected, claiming that the trustees had failed to satisfy the prudent person standard.[89] The court agreed and surcharged them for the loss of the trust corpus.[90]

B. Trust Advisors

A trust advisor has been defined as "a person who has power to control a trustee in the exercise of some or all of his powers."[91] Traditionally, trust advisors were principally concerned with overseeing the trust's investments.[92] However, trust advisors can perform other functions as well, including some that overlap with the functions performed by trust protectors.[93] Judicial decisions regarding the fiduciary duties of trust advisors are relevant in determining what the fiduciary duties of trust protectors may be when they exercise the same sort of power as a trust advisor over a

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[81] RESTATEMENT (SECOND) OF TRUSTS § 227(a) (1959).
[82] Estate of Collins, 139 Cal. Rptr. 644 (Ct. App. 1977).
[83] *Id.* at 646.
[84] *Id.* at 647.
[85] *Id.*
[86] *Id.*
[87] *Estate of Collins*, 139 Cal. Rptr. at 647.
[88] *Id.*
[89] *Id.* at 648.
[90] *Id.* at 649.
[91] *See* Harvard Law Review Association, *supra* note 32, at 1230.
[92] Ruce, *supra* note 20, at 75.
[93] *See* Duncan & Sarafa, *supra* note 33, at 781.

trustee.[94]

Stuart v. Wilmington Trust Co.[95] provides an interesting example of a trust advisor's duty of loyalty. In that case, Elbridge Stuart established a revocable inter vivos trust in 1934 that named the Wilmington Trust Company as trustee.[96] The trust agreement provided for the payment of all income from the trust to Elbridge and, at his death, a portion of the trust would be transferred to a family foundation, with the remainder to be divided among three residuary trusts.[97] An annuity funded by income from the three trusts would be paid to the settlor's son, Elbridge Hadley Stuart, during his lifetime and, at his death, the income from each of the trusts would be paid to one of the named grandsons.[98] Elbridge Hadley Stuart died in 1972 and the beneficial interest in one of the trusts vested in his son, Dwight Lyman Stuart.[99] The trust advisors of this trust were Dwight Lyman Stuart and Jane Whitman, who were appointed in 1982.[100]

Shortly thereafter, Dwight petitioned the trustee to invade the trust corpus in the amount of $4.5 million so that he could purchase a jet airplane for his personal "benefit."[101] When the other trust advisor withheld her consent, the trustee petitioned the chancery court for instructions.[102] The lower court held that since Dwight was a fiduciary, he was disqualified by virtue of his self-interest from acting and voting as a trust advisor when consenting to a discretionary invasion of the trust principal for his own benefit.[103] This decision was upheld on appeal.[104]

C. Trust Protectors

1. *Decisions from Foreign Jurisdictions*

A number of reported decisions from foreign jurisdictions have concluded that trust protectors cannot use their powers for their own benefit (unless the power is deemed to be personal), but must only act for the benefit of the trust beneficiaries.[105] The reasoning of these

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[94] *See* Bove, *supra* note 31, at 51.
[95] Stuart v. Wilmington Trust Co., 474 A.2d 121 (Del. 1984).
[96] *Id.* at 123.
[97] *Id.*
[98] *Id.*
[99] *Id.*
[100] *Stuart*, 474 A.2d at 124.
[101] *Id.* at 122.
[102] *Id.*
[103] *Id.* at 123.
[104] *Id.*
[105] *See generally* Centre Trustees (C.I.) Ltd. & Langry Trust Co. (C.I.) Ltd. v. Pabst, 2009 JLR 202 (Royal Ct. of Jersey 2009); Jurgen Von Knieriem v. Bermuda Trust Co. Ltd. and

decisions is applicable to American trust protectors as well. The seminal case in this area is *Skeats' Settlement,*[106] which was decided by the English Chancery Court in 1889. Under the terms of an 1882 marriage settlement, certain property was transferred in trust to Mary Skeats for life with a gift over to any children of the marriage.[107] The settlement also provided that if there were no children, then Mary would be given a general power of appointment.[108] Finally, the husband, Joseph Skeats, and Mary retained to the power to appoint a replacement for any trustee who died, retired, resided abroad, or became incapable of serving as a trustee.[109]

In 1889, when Evans and Bennett, two of the original trustees, decided to retire, Joseph and Mary exercised the power to replace trustees and named Joseph to be one of the trustees.[110] Evans and Bennett were doubtful that Joseph had the power to appoint himself as successor trustee, even with Mary's consent, and, therefore, refused to transfer the trust property to the new trustees without court approval.[111] Although there was no doubt that the settlor could create a power in a third party to appoint a successor trustee, it was not clear whether Joseph could validly exercise that power to appoint himself as trustee. The court declared that the validity of the appointment depended on whether the power in question was fiduciary or not.[112] The court concluded that it depended on whether the appointer or donee of the power was limited in the way he could exercise the power.[113] For example, the donee of the power could not put the office of trustee up for sale to the highest bidder.[114] According to the court:

> Suppose, as happens not infrequently, that trustees, under the terms of the deed of trust, are entitled to remuneration by way of annual salary or payment. Could the person who has the power of appointment put the office of trustee up for sale and sell it to the best bidder? It is clear that would be entirely improper. Could he take any remuneration for making the appointment? In my opinion, certainly not. Why

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Grosvenor Trust Co., *in* 1 OFFSHORE CASES AND MATERIALS 116 (Giles Clarke ed., 1996); Skeats v. Evans, 42 Ch. D. 522 (1889).

[106] *See Skeats*, 42 Ch. D. 522.

[107] *Id.* at 522.

[108] *Id.*

[109] *Id.* at 523.

[110] *Id.*

[111] *Skeats*, 42 Ch. D. at 524.

[112] *Id.* at 526.

[113] *Id.*

[114] *Id.*

> not? The answer is that he cannot exercise the power for his own benefit. Why not again? The answer is inevitable. Because it is a power which involves a duty of a fiduciary nature; and I therefore come to the conclusion, independently of any authority, that the power is a fiduciary power.[115]

Since the power to appoint a successor trustee was fiduciary in nature, the court then considered whether the donee of the power was necessarily prohibited from appointing himself.[116] Citing the maxim that "a man should not be judge in his own case," the court concluded that a donee of a power to appoint could not fairly judge his own fitness for the position as it would be inconsistent with the donee's fiduciary obligations to the settlor and the trust beneficiaries to appoint himself.[117] Accordingly, the court ruled that Joseph's attempt to appoint himself as trustee was invalid.[118]

Von Knieriem v. Bermuda Trust Co. Ltd. and Grosvenor Trust Co.[119] (also known as the Star Trusts Case),[120] suggests that some, but not necessarily all, of a trust protector's powers may be fiduciary in nature. In that case, a trust situated in Bermuda owned a substantial interest in certain pharmaceutical companies.[121] The trust instrument authorized the trust protector to appoint or remove additional trustees.[122] Litigation ensued when the trust protector removed the original trustee and appointed a new trustee.[123] Counsel for the original trustee argued that the trust protector's powers were fiduciary in nature and could only be exercised in the best interests of the beneficiaries as a whole.[124]

The court reviewed the terms of the trust and concluded that the powers conferred on the trust protector were not expressly stated to be fiduciary.[125] Nevertheless, since the trust specifically provided that the trust protector could not be a beneficiary of the trust, the court concluded that he could not exercise the power to remove and replace the trustee for his own benefit, and, for that reason, the

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[115] *Id.* at 526.
[116] *See Skeats*, 42 Ch. D. at 527.
[117] *Id.*
[118] *Id.*
[119] *See* Jurgen Von Knieriem, *supra* note 105.
[120] *See* Waters, *supra* note 21, at 65.
[121] Jurgen Von Knieriem, *supra* note 105, at 118-19.
[122] *Id.* at 119.
[123] *Id.* at 120.
[124] *See id.*
[125] *Id.* at 122.

powers were of a fiduciary nature.[126] After determining that the trust protector had not exercised the power for his own benefit, it ruled that the removal of the trustee was valid.[127]

In *Rawcliffe v. Steele*,[128] the trust instrument provided that the trust protector had to consent to any distributions to the trust beneficiaries. Since no trust protector had been appointed by the settlor, the trustee petitioned the High Court of the Isle of Man, the *situs* of the trust, to appoint a trust protector.[129] In response, the court held that since the trust protector's powers were fiduciary in nature, the appointment was subject to court supervision.[130]

Centre Trustees (C.I.) Ltd. and Langry Trust Co. (C.I.) Ltd. v. Pabst,[131] a decision from the Royal Court of the Island of Jersey, also held that a trust protector was a fiduciary, for at least some purposes. In *Centre*, the trustee sought to remove Wilfred Pabst as trust protector and appointer of a discretionary trust created by his former business associate.[132] The trust owned fifty percent of a business previously operated by the trust protector and the settlor, while the remaining fifty percent of the business was owned by a trust established by the trust protector, Pabst.[133] Certain powers of the trustee, largely those involving distributions and investments of the trust estate, could only be exercised with the consent of the trust protector.[134] In addition, the trust appointer was given the power to appoint new or additional trustees and trust protectors.[135] Finally, the trust specifically stated that "no power is vested in the protector in a fiduciary capacity."[136]

The trust protector, in his individual capacity, made certain claims against the trust.[137] According to the court, this action gave rise to a clear conflict of interest between Pabst, as the trust protector and appointer, and the trust.[138] The Jersey court noted that the trust beneficiaries were entitled to have decisions made by the trust

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[126] *See* Jurgen Von Knieriem, *supra* note 105, at 123-24.

[127] *See id.* at 125.

[128] Rawcliffe v. Steele, 1993-95 MLR 426 (High Court, Isle of Man); Ruce, *supra* note 20, at 88.

[129] *Rawcliffe*, 1993-95 MLR at 427.

[130] *Id.* at 513.

[131] Centre Trustees (C.I.) Ltd. and Langry Trust Co. (C.I.) Ltd. v. Pabst, 2009 JLR 202 (June 2, 2009).

[132] *Id.* at 204.

[133] *Id.* at 202.

[134] *Id.* at 205.

[135] *Id.*

[136] *Centre Trustees*, 2009 JLR at 211.

[137] *See id.* at 214.

[138] *Id.*

protector and the trust appointer free of any private interests or competing duties associated with the office of trust protector or trust appointer.[139] Therefore, it concluded that Pabst had a duty to resign as trust protector and trust appointer as soon as he realized that claims in which he had a personal interest would be made against the trust.[140] According to the court, the exercise of Pabst's powers as trust protector would be inextricably intertwined with his conflict of interest so that he would be unable to exercise his powers without considering the benefit to himself.[141]

2. *Domestic Statutes*

Although, section 808 of the Uniform Trust Code (hereinafter "UTC") does not mention trust protectors by name, a comment to this provision states that it applies to both trust advisors and trust protectors.[142] Furthermore, section 808(d) states that "[a] person, other than a beneficiary, who holds a power to direct is presumptively a fiduciary who, as such, is required to act in good faith with regard to the purposes of the trust and the interests of the beneficiaries."[143] The comment to sections 808(b)-(d) of the UTC indicates that these sections are intended to ratify the use of trust protectors and trust advisors.[144] However, the comment also distinguishes between trust advisors, who have "long been used for certain trustee functions, such as the power to direct investments or manage a closely-held business," and trust protectors, who often are granted greater powers, "sometimes including the power to amend or terminate the trust."[145]

The comment to section 808 also distinguishes between a power to direct, which is expressly covered by the provisions of the section, and a veto power.[146] The holder of the power to direct is able to initiate the action and direct the performance of the trustee with respect to that action.[147] In contrast, the holder of a veto power does not have the power to initiate any action, but is in the position of simply vetoing action initiated or proposed by the trustee.[148] The power to initiate seems to be directly covered by section 808, but the power to veto may not be. However, the latter power is clearly one that may be vested in a trust protector. Thus, the question arises as

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[139] *Id.*
[140] *Id.*
[141] *Centre Trustees*, 2009 JLR at 214.
[142] UNIF. TRUST CODE § 808 cmt. at 142 (2000) (amended 2010).
[143] *Id.* § 808(d).
[144] *Id.* § 808 cmt. at 142.
[145] *Id.* § 808 cmt. at 142-43.
[146] *Id.* § 808 cmt. at 143.
[147] UNIF. TRUST CODE § 808 cmt. at 143.
[148] *Id.*

to whether the Code considers the power to veto actions by the trustee, as well as other powers that may be exercised by a trust protector, to also be presumptively fiduciary in nature. Furthermore, the comment to section 808 declares that the holder of a power "can be held liable if the holder's conduct constitutes a breach of trust, whether through action or inaction."[149] Finally, the comment also declares that the provisions of section 808 can be altered by the terms of the trust.[150]

Other states have also declared trust protectors to be fiduciaries. For example, the Delaware UTC-based statute originally provided that persons who had the authority to "direct, consent to or disapprove a fiduciary's actual or proposed investment decisions, distribution decisions or other decision of the fiduciary," that is, trust advisors, were considered to be fiduciaries when exercising such authority.[151] The statute was recently amended to add new "trust protector" provisions, which delineate some of the broader powers that are commonly given to a protector, including the power to remove and appoint trustees, modify the trust instrument, and modify, expand or restrict the terms of a power of appointment.[152] Unfortunately, this provision was added to an existing statute without distinguishing between the "trust" powers that may be conferred on a trust advisor and the powers that would generally not be given to a trustee so it is not clear whether a trust protector would be a fiduciary when exercising these additional powers. A New Hampshire statute declares that a trust advisor or trust protector, other than a beneficiary, is a fiduciary and must act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.[153] This suggests that a trust protector may be considered to be fiduciary for all purposes.

A recently enacted Illinois statute designates the trust protector as a "fiduciary of the trust" who is deemed to be "subject to the same duties and standards applicable to a trustee of a trust" unless negated by the governing instrument.[154] Likewise, a Michigan law provides that, except in limited circumstances, a "trust protector is a fiduciary to the extent of the powers, duties and discretions granted to him or her under the terms of the trust . . ." and "shall act in good faith and in accordance with the terms and purposes of the

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[149] *Id.*
[150] *Id.*
[151] DEL. CODE ANN. tit. 12, § 3313(a) (2011).
[152] *Id.* § 3313(f)(1)–(3).
[153] N.H. REV. STAT. ANN. § 564-B:12-1202(a) (2008).
[154] 760 ILL. COMP. STAT. 5/16.3(e) (2013).

trust and the interests of the beneficiaries."[155] In addition, a Wyoming statute provides that trust protectors are fiduciaries to the extent of their "powers, duties and discretions granted to them under the terms of the trust."[156] This statutory language seemingly covers all functions that a trust protector is authorized to perform. Newly enacted legislation in Missouri states, somewhat ambiguously, that while a trust protector acts in a fiduciary capacity, the "trust protector is not a trustee, and is not liable or accountable as a trustee when performing or declining to perform the express powers given to the trust protector in the trust instrument."[157]

However, some statutes indicate that trust protectors may not be fiduciaries unless fiduciary status is imposed upon them in the trust instrument. For example, an Alaska statute provides that, subject to the terms of the trust instrument, "a trust protector is not liable or accountable as a trustee or fiduciary because of an act or omission of the trust protector taken when performing the function of a trust protector under the trust instrument."[158] An Arizona statute uses similar language, but another provision states that "a person, other than a beneficiary, who holds a power to direct is presumptively a fiduciary . . . ."[159] The apparent conflict between these two statutory provisions creates an ambiguous situation. An Idaho statute states that the powers of a trust protector "may, in the best interests of the trust, be exercised . . . in the sole and absolute discretion of the trust protector and shall be binding on all other persons."[160] While indicating that trust advisors with a power to direct or consent to a fiduciary's investment or distribution decisions are fiduciaries with respect to such decisions, the Idaho statute does say whether a trust protector who exercises such powers is a fiduciary as well.

In addition, a South Dakota statute provides that a trust protector "may not be considered to be acting in a fiduciary capacity except to the extent the governing instrument provides otherwise."[161] The statute also declares "[u]nless the governing instrument provides otherwise, a trust advisor or trust protector has no greater liability to any person than would a trustee holding or benefitting from the rights, powers, privileges, benefits, immunities, or authority provided or allowed by the governing instrument to such trust advisor or trust

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[155] MICH. COMP. LAWS § 700.7809(1)(a)–(b) (2010).
[156] WYO. STAT. ANN. § 4-10-711 (2003).
[157] MO. REV. STAT. §456.8-808(6)(1) (2012).
[158] ALASKA STAT. § 13.36.370(d) (2013).
[159] ARIZ. REV. STAT. ANN. § 14-10808(D)(2).
[160] IDAHO CODE ANN. § 15-7-501(6) (2013).
[161] S.D. CODIFIED LAWS § 55-1B-1 (2011).

protector."[162] This statute does differentiate between a trust protector exercising the authority of an investment trust advisor or a distribution trust advisor, where the protector would be acting in a fiduciary capacity, and a trust protector exercising other (i.e. non-fiduciary) powers.[163]

The UTC and a number of state statutes indicate that trust protectors are to be considered fiduciaries in the exercise of some or all of their functions unless the trust instrument provides otherwise. However, this view is not a universal one. A few statutes take the opposite position and declare that trust protectors are normally not fiduciaries.

3. *The* McLean *Case*

Robert T. McLean Irrevocable Trust[164] is the only American case to consider whether a trust protector is subject to any fiduciary duties. The *McLean* case involved a special needs trust created for Robert McLean from the proceeds of his personal injury settlement.[165] Under the terms of the trust, the trust protector was given the power to remove the trustee and to appoint a trustee to replace the removed trustee or whenever the office of trustee became vacant.[166] The trust further provided that "[t]he Trust Protector's authority hereunder is conferred in a fiduciary capacity and shall be so exercised," but went on to declare that "the Trust Protector shall not be liable for any action taken in good faith."[167]

The Merrill Lynch Trust Company and David Potashnick were initially appointed to serve as trustees, but both resigned within a month or so after the creation of the trust.[168] Michael Ponder, who had been appointed as the trust protector, then appointed Patrick Davis the successor trustee.[169] However, within two years after being appointed, both Davis and Ponder resigned and a new trustee and trust protector had to be appointed.[170] The successor trustee, after serving for less than a year, also resigned and McLean's mother was eventually appointed to serve as a successor trustee.[171] McLean's

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[162] *Id.* § 55-1B-1.1.
[163] *Id.* § 55-1B-1.
[164] Robert T. McLean Irrevocable Trust v. Patrick Davis, P.C., 283 S.W.3d 786 (Mo. Ct. App. 2009).
[165] *Id.* at 789.
[166] *Id.* at 790.
[167] *Id.*
[168] *Id.* at 789.
[169] *McLean*, 283 S.W.3d at 790.
[170] *Id.*
[171] *Id.*

mother brought suit against Ponder, alleging, *inter alia*, that the trust protector had a duty to monitor the actions of the trustee to see whether he was properly administering the trust.[172] The plaintiff also claimed that the trust protector had a duty to remove the trustee if he concluded that the trustee was not properly administering the trust.[173]

In reviewing the trial court's dismissal of the suit against Ponder, the standard on appeal required the appellate court to review the record in the light most favorable to the appellant, resolving all factual disputes in her favor as if the allegations were true.[174] The record on appeal consisted of the allegations in the petition, together with a copy of the trust, a very brief statement of uncontroverted facts, and a couple of affidavits.[175] The issue before the appellate court was whether there was an adequately pled breach of fiduciary duty claim before the court.[176] In other words, had Ponder presented in his statement of uncontroverted facts and affidavits any uncontroverted facts that would negate any one of the four elements of such a claim?[177] Ponder argued that he had negated two of the four elements: (1) whether the trust protector had a duty to monitor or supervise the trustees and (2) whether his failure to do so resulted in a financial loss to the trust.[178]

The appeal was held before a three-judge panel and each judge wrote a separate opinion.[179] They agreed only that the summary judgment was not appropriate because the allegations in the petition, which were disputed by Ponder, created an issue of fact and Ponder might be liable if McLean were able to prove his version of the facts.[180] Judge Burrell observed that the trust agreement appointed Ponder to serve "in a 'fiduciary capacity'" and provided limited liability "for actions taken in bad faith."[181] He also ruled that there were "significant and contested issue[s] of material fact" regarding whom the trust protector was to act in a fiduciary capacity for—the trust,

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[172] *Id.* at 790-91.

[173] The plaintiff originally filed suit against all of the prior trustees and trust protectors. However, after the suit was filed, the trial court granted a motion to dismiss and a motion for summary judgment made by Ponder, the original trust protector. After Ponder's dismissal from the case, the remaining defendants apparently settled, leaving Ponder as the sole remaining defendant on appeal. *Id.* at 792.

[174] *McLean*, 283 S.W.3d at 788.

[175] *Id.* at 788-89.

[176] *Id.* at 792.

[177] *Id.* at 792-93.

[178] *Id.* at 793.

[179] *See McLean*, 283 S.W.3d. at 795-96.

[180] *Id.* at 792.

[181] *Id.* at 794 (emphasis omitted).

the settlor, or the beneficiary—and what the intent of the settlor was, which was not clearly set out in the trust agreement.[182] Judge Burrell also stated that he was not deciding that there was a duty of care and loyalty that was breached; only that there were material issues of fact as to the elements of a claim for breach of fiduciary duty and that McLean should have the opportunity to prove the elements of breach of fiduciary duty alleged in his petition.[183]

In addressing the causation issue, Judge Burrell concluded that the trust protector had not presented any uncontroverted facts that would have established that the beneficiary, as a matter of law, would have been entitled to a judgment removing the trustee.[184] He also pointed out that "[b]ecause no legal duties for a trust protector have been imposed by the Missouri legislature, any such duties may only arise from the nature of the relationship between the parties or the language of the trust."[185] Based on the language of the trust instrument, Judge Burrell concluded that there could be "an inference that the Trust Protector could be susceptible to liability for actions taken in bad faith" if the appellant was able to prove each of the allegations in the petition.[186]

Each of the other two judges hearing the case wrote a concurring opinion, reluctantly concurring in the result only.[187] The concurring opinion of Judge Parrish relied solely on the terms of the trust instrument to ascertain the scope of any duty that might exist for the trust protector, concluding that "absent the trust protector doing something in bad faith, he is not liable for his conduct."[188] However, Judge Parrish also determined that since McLean had alleged in his petition that the trust protector had acted in bad faith, he raised a factual issue that precluded the granting of a summary judgment in favor of the trust protector.[189] In her concurring opinion, Judge Rahmeyer stated that:

> I agree that there is no duty as a matter of law as a 'trust protector,' but I do not agree that as a matter of law the duty of the Trust Protector [in this case] was to the beneficiary, at least not in the traditional sense, nor do I equate the right to remove trustees and appoint successors with a duty to remove trustees and

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[182] *Id.* at 795.
[183] *Id.*
[184] *McLean*, 283 S.W.3d at 793.
[185] *Id.* at 794.
[186] Id at 795.
[187] *See id.* at 795-96 (Parrish, J. & Rahmeyer, J., concurring).
[188] *Id.* at 796 (Parrish, J., concurring).
[189] *McLean*, 283 S.W.3d at 796 (Parrish, J., concurring).

appoint successor trustees.[190]

However, Judge Rahmeyer stated that it was not appropriate for the court to "make up the duties of a trust protector out of whole cloth" and for this reason held that the trial court erred in granting summary judgment on the record before it.[191]

Since the holding in the case deals solely with whether the trust protector's motion to dismiss, or in the alternative for a motion for summary judgment, was properly granted by the trial court, the appellate court's principal concern was whether the allegations in the scant pleadings before the trial court, if taken as true, could have formed a sufficient basis for liability.[192] For that reason, the court's observations of the powers, duties, and liabilities of trust protectors must be regarded as *dicta*.

The case was eventually sent back to the trial court, where the parties conducted extensive discovery and filed numerous motions.[193] Prior to trial, in the process of ruling on cross motions *in limine* to limit expert testimony, the trial court issued an opinion as to the law applicable to the case. In the order issued, the trial court quoted from the prior appellate court opinion that "the question of whether a duty exists is a question of law and, therefore, a question for the court alone."[194] The circuit court judge, Michael Pritchett, then indicated to counsel in granting the motions *in limine* before him, that he would not permit expert testimony regarding Ponder's legal duties as trust protector.[195]

In ruling on the pretrial motions, Judge Pritchett stated that the role of a trust protector is separate and distinct from the role of a trustee.[196] After reviewing the trust provisions concerning the trust protector and also concerning the trustee for the McLean Trust, the trial court ruled that while the trust protector had the authority to remove a trustee, the trustee was not required to submit any accountings to the trust protector because the trustee was independent of the control or supervision of the trust protector and

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[190] *Id.* (Rahmeyer, J., concurring).

[191] *Id.*

[192] *McLean*, 283 S.W.3d at 788.

[193] Robert T. McLean Irrevocable Trust v. Ponder, No. 36V010500665-01 (Mo. Cir. Ct. Oct. 20, 2011).

[194] *Id.* at 1 (quoting Robert T. McLean Irrevocable Trust v. Patrick Davis, P.C., 283 S.W.3d 786 (Mo. Ct. App. 2009)).

[195] Robert T. McLean Irrevocable Trust v. Ponder, 418 S.W.3d 482, 499 (Mo. Ct. App. 2013), *reh'g and/or transfer denied* (Nov. 15, 2013), *transfer denied* (Feb. 25, 2014).

[196] *See* Robert T. McLean Irrevocable Trust v. Ponder, No. 36V010500665-01, 1 (Mo. Cir. Ct. Oct. 20, 2011).

because the trust protector has no veto power over the conduct of the trustee.[197] The court then ruled that the trust protector had no obligation to monitor the activities of the trustee, but also declared that:

> [T]he Trust Protector could [not] simply ignore conduct of a Trustee which threatened the purposes of the trust. To the extent that any conduct took place, and to the extent that the Trust Protector was made aware of any such conduct, a duty may have arisen by the Trust Protector in his fiduciary capacity to remove a trustee.[198]

The case proceeded to trial. The trial commenced on October 25, 2011, and the plaintiff rested on October 28. At that time, the defendant filed a motion for directed verdict, which the court sustained.[199] At the close of the Trust's evidence, the court granted Ponder's motion for a directed verdict.[200] The Trust again appealed to the Missouri Court of Appeals.[201]

In its appeal, the Trust identified eleven alleged errors on the part of the trial court that it claimed supported a reversal of the lower court's judgment. These included:

> (1) dismissing claims of Robert individually and Linda as Trustee, as barred by the statute of limitations, or if barred, the statute of limitations was tolled due to Robert's incapacity; (2) failing to articulate the proper standard of care for fiduciaries; (3) granting Ponder's motion because the Trust 'presented a submissible case'; (4) granting Ponder's Motion because the trial court 'failed to acknowledge [Ponder's] involvement in the creation and administration of the Trust and their attorney client relationship'; (5) requiring the Trust to prove bad faith; (6) excluding expert testimony of Menees; (7) excluding expert testimony of Bove; (8) issuing a 'withdrawel [sic] instruction' regarding the testimony of James McClellan ("McClellan"); (9) excluding and disregarding testimony of Linda as to the 'wrongful exclusion of [Robert] from the trust

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[197] *See id.* at 3.

[198] Robert T. McLean Irrevocable Trust v. Ponder, No. 36V010500665-01, 3 (Mo. Cir. Ct. Oct. 20, 2011).

[199] *Id.*

[200] *Id.* at 1.

[201] Robert T. McLean Irrevocable Trust v. Ponder, 418 S.W.3d 482 (Mo. Ct. App. 2013), *reh'g and/or transfer denied* (Nov. 15, 2013), *transfer denied* (Feb. 25, 2014).

> property'; (10) substituting 'its own judgment for that of the fact finder finding against the weight of the evidence on facts based on erroneous legal reasoning as Respondents [sic] affirmative defenses were legally inapplicable and should have been stricken' [and ample evidence of damages and causation was submitted to the court]; and (11) 'entering a judgment for Ponder because the verdict is only against the weight of the evidence but as made without the evidence and the cumulative affect [sic] of the courts [sic] rulings were against the weight of the evidence and indicate a judicial bias and deprived [the Trust] of a fair trial.'[202]

The appeals court first considered point ten in which the Trust alleged that it had presented evidence that the Trust had suffered economic harm as the result of Ponder's failure to remove the trustee in December 1999.[203] According to the Trust, the Trust eventually lost more than $500,000 as a direct result of Ponder's failure to remove the Trustee.[204] However, the court concluded that the Trust had failed to provide any specific evidence of loss to the Trust that could have been prevented by timely removal of the trustee by Ponder.[205]

Next the court addressed points two through five and concluded that they were moot since the Trust had failed to prove any damages attributable to Ponder's action or inaction.[206] Point one challenged the trial court's dismissal of certain individual claims of Robert and Linda McLean.[207] However, the appeals court determined that neither Robert nor Linda McLean, in their individual capacities, had appealed the lower court's decision after the first trial in 2007.[208] Therefore, only the Trust remained as a party after that time.[209] Consequently, the court upheld the trial court's dismissal of the McCleans' individual claims.[210] The appeals court also rejected the Trust's contention in points eight and nine that the trial court erred in refusing to allow testimony regarding Ponder's refusal to allow Robert McLean permission to return to his residence, which was owned by the Trust.[211] The trial court concluded that testimony about

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[202] *Id.* at 488.
[203] *Id.* at 490.
[204] *Id.*
[205] *Id.* at 490-96.
[206] Robert T. McLean Irrevocable Trust, 418 S.W.3d at 497.
[207] *Id.*
[208] *Id.* at 498.
[209] *Id.*
[210] *Id.*
[211] Robert T. McLean Irrevocable Trust, 418 S.W.3d at 498-99.

the exclusion of Robert from his residence was not relevant to any economic damage claim by the Trust.[212]

Points six and seven involved the trial court's exclusion of expert testimony by Alexander Bove and Hardy Menees proffered by the Trust regarding Ponder's duties as a trust protector.[213] The appeals court rejected the Trust's claim of error by the trial court because it found that the Trust had simply made a bare assertion that the trial court erred and failed to provide any factual or legal basis context for the alleged error.[214] Finally, the court rejected the Trust's 11th point because it combined allegations of error not related to a single issue in violation of section 84.04 of the Missouri Rules of Appellate Procedure.[215]

Unfortunately, this latest development in the *McLean* saga sheds very little light on what a trust protector's fiduciary duties might be. By concluding that the Trust failed to prove that it suffered any damage as a result of Ponder's failure to remove the trustee, the court was able to avoid deciding whether Ponder was a fiduciary (though it implicitly assumed that he was), what the nature of his duties to the Trust might be, and whether these fiduciary duties, if any, were inherent in the office of trust protector or whether they arose solely from the trust instrument. In addition, the court did not have to decide whether Ponder had a duty to actively oversee or supervise the actions of the trustee.

D. Conclusion

There is a considerable body of legal authority that indicates that trust protectors are subject to fiduciary duties. At the very least, a trust protector must act solely for the benefit of the trust beneficiaries and cannot use his or her powers for personal benefit. In other words, a trust protector owes a duty of loyalty to trust beneficiaries that is similar to that owed by trustees. There is also legal authority, partly based on decisions involving trust advisors that dictates that trust protectors be treated as fiduciaries when they exercise powers that are generally exercised by trustees. On the other hand, it is less clear whether trust protectors act as fiduciaries when they exercise powers that are not ordinarily exercised by trustees.

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[212] *Id.* at 499.
[213] *Id.*
[214] *Id.* at 499-50.
[215] *Id.* at 500.

III. ANALYSIS

There is no reason why the settlor and a trust protector cannot agree that the trust protector will be subject to certain fiduciary duties. A more difficult issue is whether trust protectors should be subject to fiduciary duties in the absence of such an agreement. As mentioned earlier, trustees are subject to a number of fiduciary duties, such as loyalty, prudence, and impartiality under ordinary principles of trust law, even in the absence of an express agreement.[216] Are trust protectors any different? In order to determine whether any fiduciary duties should be imposed on trust protectors, it is necessary to consider a number of questions. First, should courts or legislatures impose any fiduciary duties on trust protectors at all? Second, if so, should trust protectors be subject to certain minimum standards of conduct in the exercise of *all* of their powers and functions or only in the exercise of some of them? Third, if a trust protector is a fiduciary, what minimum standards of conduct should be applicable to his conduct? Fourth, should a higher standard of conduct be applied to certain powers exercised by trust protectors? Fifth, to what extent should the settlor be allowed to increase or waive the default standard of conduct? Sixth, who would have standing to sue a trust protector for breach of fiduciary duty? Finally, what sanctions should be imposed on a trust protector for breach of a fiduciary duty?

A. Is a Trust Protector Ever a Fiduciary?

A strong case can be made that trust protectors should be considered fiduciaries, at least for some purposes. First of all, there is considerable authority in foreign jurisdictions for this position and the reasoning of these cases is quite persuasive. For example, in the *Skeats' Settlement* case,[217] the English Chancery Court concluded that there must be some limit on the exercise of power by a trust protector or else he would be free to personally profit from the exercise of that power at the expense of the trust beneficiaries.[218] Thus, if a trust protector who was given the power to appoint and remove trustees was free to sell that office to the highest bidder or to receive a share of the trustee's compensation, a trustee who was appointed in this manner, would not be expected to act in the best interests of the beneficiaries.

A similar theme runs through some of the other cases discussed in Part II. For example, in the *Von Knieriem* case, the Bermuda High Court agreed with the reasoning of *Skeats* that a trust

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[216] *See supra*, Part II.A.

[217] *See* Skeats v. Evans, 42 Ch. D. 522 (1889).

[218] *Id.* at 526.

protector was a fiduciary, at least for some purposes, because he could not exercise the power to appoint and replace trustees for his own benefit.[219] Also, in *Centre Trustees (C.I.) Ltd. & Langry Trust Co. (C.I.) Ltd. v. Pabst*, the Royal Court of the Island of Jersey held that even though the trust protector was not obliged to exercise certain powers under the trust, the powers were still fiduciary in nature because if he did exercise them, he must do so on behalf of the beneficiaries of the trust.[220]

There is statutory support for this position as well. Section 808 of the Uniform Probate Code declares that one who holds a power to direct (such as a trust advisor or trust protector), is presumptively a fiduciary.[221] Other statutes are even more explicit. For example, statutes in Delaware,[222] New Hampshire,[223] Illinois,[224] Michigan,[225] Wyoming,[226] and Missouri[227] provide that trust protectors will be treated as fiduciaries, at least in some circumstances. Finally, there is considerable authority for the proposition that trust advisors have traditionally been held to fiduciary standards. Since there is considerable overlap between the role of trust advisors and trust protectors, arguably the latter group should be treated as fiduciaries when they exercise similar powers.[228]

However, some jurisdictions leave it entirely up to the settlor to determine what, if any, fiduciary duties should be imposed on a trust protector. This view is reflected in statutes that have been enacted in Alaska,[229] Arizona,[230] Idaho,[231] and South Dakota.[232] These statutes declare that a trust protector will not be treated as a fiduciary unless the trust instrument so provides. This approach seems to have originated in the laws of foreign jurisdictions governing offshore asset protection trusts that been imported into some American trust protector statutes.[233] Considering that American trust

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[219] *See* Jurgen Von Knieriem, *supra* note 105; *Skeats*, 42 Ch. D. 522.

[220] *See* Centre Trustees (C.I.) Ltd. & Langry Trust Co. (C.I.) Ltd. v. Pabst, 2009 JLR 202 (Royal Ct. of Jersey, June 2, 2009).

[221] UNIF. PROBATE CODE § 3-808 (1969) (amended 2010).

[222] DEL. CODE ANN. tit. 12, § 3313 (2011).

[223] N.H. REV. STAT. ANN. § 564-B:12-1202(a) (2008).

[224] 760 ILL. COMP. STAT. 5/16.3 (2013).

[225] MICH. COMP. LAWS § 700.7809 (2010).

[226] WYO. STAT. ANN. § 4-10-711 (2003).

[227] MO. REV. STAT. § 456.8-808 (2012).

[228] *See* Bove, *supra* note 31, at 51.

[229] ALASKA STAT. 13.36.370(b) (2013).

[230] ARIZ. REV. STAT. ANN. § 14-10818(D) (2013).

[231] IDAHO CODE ANN. § 15-7-501(6) (2007).

[232] S.D. CODIFIED LAWS § 55-1B-1 (2011).

[233] *See* Bove, *supra* note 31, at 53.

protectors typically have greater powers and duties than their overseas counterparts, the better view seems to be that they should be presumptively considered fiduciaries.

B. Should Trust Protectors Be Held to Minimum Standards of Conduct for All of Their Actions?

As mentioned earlier, there is some statutory support for the proposition that trust protectors should be treated as fiduciaries for all purposes. For example, statutes in Delaware,[234] New Hampshire,[235] Illinois,[236] Michigan,[237] Wyoming,[238] and Missouri[239] provide that trust protectors will be treated as fiduciaries when exercising their powers under the trust instrument unless the settlor provides otherwise. On the other hand, several court decisions from foreign jurisdictions have ruled that trust protectors may be treated as fiduciaries for some purposes, but not necessarily for other purposes.[240]

There are several potential exceptions to the application of general standards of conduct to trust protectors. For example, several statutes,[241] as well as the Uniform Trust Code,[242] exempt trust protectors who are also trust beneficiaries from the fiduciary duties that apply to other trust protectors. The comment to section 808 of the UTC suggests that this exemption is primarily applicable to self-directed accounts such as employee benefit plans and individual retirement accounts.[243] Clearly, there is no need to impose a fiduciary duty in a case where the sole beneficiary of a trust has the power to direct how the trust assets are invested or distributed. On the other hand, if a trust protector is only one of several beneficiaries, it seems that he should be subject to minimal fiduciary duties just as a trustee or trust advisor would be who was also one of the trust beneficiaries.

Another issue is whether a trust protector should be held to a fiduciary standard only when he acts affirmatively. The Royal court of Jersey recently made this distinction in the *Centre Trustees* case.[244]

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[234] DEL. CODE ANN. tit. 12, § 3313 (2011).
[235] N.H. REV. STAT. ANN. § 564-B:12-1202(a) (2008).
[236] 760 ILL. COMP. STAT. 5/16.3 (2013).
[237] MICH. COMP. LAWS § 700.7809 (2010).
[238] WYO. STAT. ANN. § 4-10-711 (2003).
[239] MO. REV. STAT. § 456.8-808 (2012).
[240] *See* Jurgen Von Knieriem, *supra* note 105, at 118-19; Skeats v. Evans, 42 Ch. D. 522, 526 (1889).
[241] ARIZ. REV. STAT. ANN. § 14-10818(A) (2013); N.H. REV. STAT. ANN. § 564-B:12-1202(a) (2008).
[242] UNIF. TRUST CODE § 808(d) (2000) (amended 2010).
[243] *Id.* § 808, cmt.
[244] See Centre Trustees (C.I.) Ltd. & Langry Trust Co. (C.I.) Ltd. v. Pabst, 2009 JLR 202

In that case, the trust instrument declared that the powers vested in the trust protector were not held in a fiduciary capacity.[245] However, the court interpreted this to mean that the trust protector was not obliged to exercise them.[246] Although it is a close call, the better approach is to impose the minimum standards described above on decisions not to exercise a particular power. It is hard to justify a rule that would protect a trust protector from liability who refused to act solely from improper motives.

C. What Should These Minimum Standards of Conduct Be?

Assuming that trust protectors can be fiduciaries, at least in some circumstances, the next question is whether any minimum standards of conduct should be imposed, either by statute or by judicial decision, that would be applicable to all activities and functions of a trust protector (unless a higher standard of conduct is otherwise applicable). I believe that trust protectors should be subject to certain standards of conduct that reflect the fundamental principle that a fiduciary should not act to benefit himself, but rather he should act solely to advance or protect the interests of the trust beneficiaries. In addition, trust protectors should be expected to carry out the objectives of the trust and should not violate any of its express provisions. A trust protector should also be required to act in good faith and not out of spite, malice, or other improper motive. Finally, a trust protector should exercise independent judgment in the exercise of his powers. All of these moral imperatives can be captured in a formulation that is set forth in several state statutes, namely that a trust protector act in good faith and exercise independent judgment in accordance with the terms and purposes of the trust and the interests of the beneficiaries.[247] I will henceforth refer to this formulation as the "good faith" standard.

The duty to act in accordance with the terms and purposes of the trust is embodied in the duty of loyalty. It requires a trust protector to faithfully carry out the intent of the settlor as set forth in the trust instrument.[248] Where appropriate, the grantor's written instructions may be supplemented by any personal knowledge that the trust protector may have of the grantor's wishes and objectives as long as they do not directly contradict the terms of the trust. The duty to act solely in the best interests of the trust beneficiaries also

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(Royal Ct. of Jersey, June 2, 2009).

[245] *See id.*

[246] *See id.*

[247] *See* MICH. COMP. LAWS § 700.7809 (2010); N.H. REV. STAT. ANN. § 564-B:12-1202(a) (2008).

[248] *See* Hill, *supra* note 44, at 832.

involves the duty of loyalty. [249] Like trustees, trust protectors must act to further the best interests of the trust beneficiaries and must treat each beneficiary fairly.

The duty to act in good faith is somewhat more elusive. As the court in *Hartman v. Baker*[250] pointed out, "good faith" is "[a] state of mind consisting in (1) honesty in belief or purpose, (2) faithfulness to one's duty or obligation, (3) observance of reasonable commercial standards of fair dealing in a given trade or business, or (4) absence of intent to defraud or to seek unconscionable advantage."[251] When applied to trust protectors, the concept of good faith would require a trust protector to carry out his duties honestly and competently and not act out of greed, malice, or some other improper motive.

Arguably, a requirement that a trust protector exercise independent judgment is implicit in the duty of loyalty and good faith. However, a recent experience suggests that the obligation to exercise independent judgment should be set forth as an independent fiduciary duty. Recently, I was asked to advise counsel for a trust beneficiary in a case where the trustee of an *inter vivos* trust had been given the power by the settlor to appoint or remove the trust protector. The trustee, who was a beneficiary, was engaged in a long-running dispute with some of the other trust beneficiaries. The trust protector had the power to modify the terms of the trust but no trust protector had been appointed when the trust was created. However, sometime later, the trustee appointed a business associate as trust protector. The next day, the trust protector modified the trust instrument by inserting an *in terrorem* clause purporting to terminate the beneficial interest of any beneficiary who challenged the conduct of the trustee in court. The trust protector also added a provision to the trust instrument that purported to exonerate both the trustee and the trust protector from liability for any breach of trust. These provisions had been drafted by the trustee's counsel, not by the trust protector. Immediately after the trust instrument was changed, the trustee removed the trust protector. It appears that in this case, the trust protector did not exercise independent judgment when he exercised his power to modify the terms of the trust, but rather acted as an agent of the trustee. The facts of this case suggest that an explicit requirement that the trust protector exercise independent judgment ought to be included in any formula that purports to identify a trust protector's minimum standard of conduct.

The standards that I have proposed seem particularly

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[249] *Id.*

[250] Hartman v. Baker, 766 A.2d 347 (Pa. Super. Ct. 2000).

[251] *Id.* at 355 n. 3.

appropriate to individual trust protectors who are relatives or friends of the settlor and serve for little or no compensation. Should "professionals" who serve as trust protectors (assuming there are any) be held to higher standards of conduct? The Restatement of Trusts declares that if a "trustee possesses, or procured appointment by purporting to possess, special facilities or greater skill than that of a person of ordinary prudence, the trustee has a duty to use such facilities or skill."[252] Under these limited circumstances, it seems proper to hold a trust protector to a higher standard of skill and competence, particularly where he has the power to direct the management and investment of trust property.

D. Should a Higher Standard of Conduct Be Applied to Some of the Powers Exercised by Trust Protectors?

Trust protectors can be appointed to perform a variety of tasks.[253] However, most of these powers fall into one of four basic categories: (1) providing advice to trustees; (2) overseeing the activities of trustees; (3) resolving or mediating disputes; and (4) modifying or terminating the trust.[254] These powers are different in nature and, therefore, different standards of conduct could logically be applied to their exercise.

1. Advising the Trustee

The trust instrument may authorize a trust protector to advise the trustee on various matters of trust administration. This power should be distinguished from the power to direct, where the trustee is required to follow the trust protector's directions. This advisory power could extend to a variety of issues, including investment decisions, discretionary distributions, or when and how to provide financial information to qualified beneficiaries. Obviously, some of the advice provided by the trust protector may require financial or legal expertise on the part of the trust protector, while other advice may be based on personal knowledge of the beneficiaries and their circumstances. In the former case, one could argue that a trust protector be held to a professional standard of care. Otherwise, a "good faith" standard seems appropriate.

2. Supervising the Activities of the Trustee or Exercising Trustee Powers

Overseeing the conduct of the trustee was one of the major functions of trust protectors during the early days of offshore asset

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[252] RESTATEMENT (THIRD) OF TRUSTS § 77(3) (2007); *see* UNIF. TRUST CODE § 806 (2000) (amended 2010).

[253] Ruce, *supra* note 20, at 74.

[254] *See* Ausness, *supra* note 40, at 329.

protection trusts. Although it is less likely that a trust protector will be expected to act as a watchdog in the case of domestic trusts, there are some commonly held powers that are essentially supervisory in character. For example, the trust instrument may authorize the trust protector to review and approve the accountings of a trustee. In addition, it should allow the trust protector to direct, consent, or veto a trustee's action or inaction in making distributions to trust beneficiaries. Perhaps most significant of these supervisory powers is the power to appoint or remove trustees or successor trustees. Because these are discretionary powers, a "good faith" standard should be sufficient to protect the interests of the trust beneficiaries.

3. Resolving or Mediating Disputes

It is sometimes useful to empower the trust protector to interpret the terms of the trust instrument at the request of either the trustee or the beneficiaries. Depending on the terms of the trust instrument, the trust protector's interpretation can be either binding or advisory. The advantage of vesting this power in a trust protector is that it may enable the trust to avoid having to resolve disputes that would otherwise have to be decided by litigation.[255] A trust protector can also act as a mediator between the trustee and the trust beneficiaries when disputes arise between or among them.[256] Once again, due to the discretionary nature of these powers, a "good faith" standard seems best suited to the exercise of these powers.

4. Modifying or Terminating the Trust

One method of achieving flexibility with respect to "irrevocable" trusts is to empower a trust protector to modify either administrative or substantive provisions of the trust. The power to amend administrative provisions is often limited to specific situations, such as changing the provisions of the trust to achieve a more favorable tax status or to take advantages of changes in the law of property, trusts, or trust administration. In addition, the trust instrument may empower the trust protector to modify the trust's administrative provisions, including changing the governing law of the trust or moving the *situs* of the trust to another state.

In addition, the trust instrument may authorize the trust protector to modify the substantive provisions of the trust. This power may include the right to increase or decrease the interest of any trust beneficiary, the right to grant a power of appointment to a trust beneficiary or to terminate or amend a power of appointment, to

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[255] *See* Jeffrey Evans Stake, *A Brief Comment on Trust Protectors*, 27 CARDOZO L. REV. 2813, 2814-15 (2006).

[256] Ruce, *supra* note 20, at 72.

convert the trust to a spendthrift trust, or the right to terminate the trust and distribute the trust corpus to the beneficiaries. Although the trustee or the beneficiaries can petition a court to change the terms of the trust, judicial reformation can be expensive.[257] Vesting this power in a trust protector can avoid much of this expense. In some cases, the exercise of these powers might require expertise as, for example, modifying trust provisions to take advantage of changes in the tax law or transferring the *situs* of the trust to another state. In such cases, it might be desirable to hold the trust protector to a professional standard of care if he is a professional. However, for discretionary acts that do not require such expertise, the "good faith" standard, once again, seems to be appropriate.

To conclude, a strong argument can be made that a trust protector's fiduciary standard of conduct should vary according to the function or power being exercised. Thus, one can argue that a trust protector who provides professional advice on legal or financial matters should be held to a professional standard of care. Likewise, when a trust protector exercises powers that would ordinarily be reserved to a trustee, it seems reasonable to impose the same fiduciary standards on the trust protector that would be imposed by law on a trustee. However, for discretionary acts, a "good faith" standard is the best approach.

E. Modification of Minimum Fiduciary Duties in the Trust Instrument

I have concluded that trust protectors should be subject to a legislatively or judicially imposed minimum standard of conduct. At the same time, settlors should be free to impose higher standards in connection with the exercise of certain powers if they choose. However, should settlors also be able to relieve a trust protector of all fiduciary duties? Presumably, they could do so by specifying that some or all of the powers authorized in the trust instrument are deemed to be personal and not held in trust.[258] If a trust protector's power is personal in nature, the power is purely discretionary and an "individual holding a personal power cannot be forced to exercise it and in fact need not even consider whether to exercise it. And if he does exercise such a power, he may do so on a whim, or even for a spiteful or malicious reason, so long as he does not commit a fraud on the power."[259] However, it is difficult to conclude that a rational settlor would want to confer this sort of power on a disinterested third

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[257] *Id.* at 70.

[258] *Id.* at 80-81.

[259] Alexander A. Bove, Jr., *The Trust Protector: Trust(y) Watchdog or Expensive Exotic Pet?*, 30 EST. PLAN. 390, 391 (2003) [hereinafter *"Trust(y) Watchdog"*].

party. On the other hand, if a settlor wishes to give an unfettered power to a child or spouse, it might be better (tax considerations aside) to transfer the power to the person outright instead of appointing him or her to be a trust protector.

F. Sanctions for Breach of Fiduciary Duty

What sort of sanctions should a court impose on a trust protector who has breached a fiduciary duty? Presumably, the same remedies that are available for breach of fiduciary duty by a trustee would also be available where a trust protector breached a fiduciary duty. For example, a court could order a trust protector to carry out a duty or exercise a power if it were mandatory in nature. A court could also reverse an action by a trust protector that violates a fiduciary duty and order him to return matters to the *status quo ante*. In addition, a court could remove a trust protector if the breach is flagrant or prolonged. Finally, a court might award damages if the trust protector's breach of fiduciary duty results in a financial loss to the trust or its beneficiaries.

In most cases, the trust beneficiaries would have standing to bring an action against the trust protector for breach of fiduciary duty.[260] It is also possible that the trustee would be able to proceed against a trust protector for breach of fiduciary duty if the beneficiaries fail to act.[261] Finally, a settlor who is still alive and has retained an interest in the trust may also have standing to sue the trust protector for breach of trust.

IV. DRAFTING ADVICE

Because the nature, and in some cases even the very existence, of a trust protector's fiduciary duties may not be clearly addressed by statute or judicial decision, it is essential to consider this issue fully in the trust instrument. In particular, the drafter should: (1) enumerate each of the trust protector's powers and responsibilities; (2) identify the applicable standards of conduct; (3) provide for the appointment, removal, and compensation of trust protectors; and (4) consider whether to include an exculpatory clause in the trust instrument.

A. Enumerate Each of the Trust Protector's Powers and Responsibilities

Unlike trustees, trust protectors appear to have no inherent or implied powers. In some states, the powers of a trust protector are set forth (usually on a non-exclusive basis) by statute. However, even in

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[260] *See* Bove, *supra* note 31, at 52.
[261] *Id.*

those states, it is good practice to identify in the trust instrument the specific powers that the settlor wants the trust protector to have. That way, the trust protector will only be allowed to exercise the powers that are necessary to carry out the objectives of the trust. In addition to enumerating specific powers, the drafter should consider requiring the trustee to provide the trust protector, when necessary, with periodic reports regarding the administration of the trust, as well as access to accounting and tax information.[262]

Another consideration is whether to grant a particular power to the trust protector without any conditions or limitations, or whether to limit the exercise of a power to a special set of circumstances. Limiting the exercise of a particular power provides greater protection against abuse of power by the trust protector. However, it also increases the chances that a beneficiary may claim that the trust protector exceeded his authority under the terms of the trust. It goes without saying that it is essential for the drafter explain to the settlor the costs and benefits of various alternatives and to work closely with the settlor to ensure that the trust instrument fully and accurately reflects the settlor's objectives.

Finally, in addition to identifying the trust protector's powers and duties, the drafter should specify which powers, if any, are to be considered personal in nature and which are considered to be held in trust. As discussed earlier, personal powers are not fiduciary in nature. In such cases, the only limitation on the exercise of a personal power is that the donee of the power cannot act in a way that constitutes a fraud on the power.[263]

B. Identify the Applicable Standards of Conduct

Even if an applicable statute declares that a trust protector is a fiduciary, it is still desirable for the trust instrument to declare when (or if) the trust protector is a fiduciary and to specify what standard of conduct is applicable.[264] As suggested earlier, an appropriate formula would provide that the trust protector in the exercise (or non-exercise) of his powers is required to act in good faith, in accordance with the terms of the trust, in and the interests of the beneficiaries, and exercise independent judgment when carrying out his duties. These four requirements reflect the essence of a fiduciary relationship. They are suitable standards of conduct for most of the powers that a trust protector is likely to exercise and they are

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[262] *See* Carla S. Ranum & Elizabeth L. Mathieu, *Trust Protectors—A Pandora's Box?*, 55 ADVOCATE 36, 38 (Aug. 2012).

[263] *See Trust(y) Watchdog*, *supra* note 259, at 391.

[264] Charles D. Fox IV, *How "Revocable" Is "Irrevocable"? Obtaining Flexibility in Irrevocable Trusts*, 33 OHIO N.U.L. REV. 943, 956 (2007).

particularly appropriate for powers that require the trust protector to exercise discretion.

However, if a trust protector is expected to offer professional advice on legal or financial matters in addition to performing other functions, the settlor might wish to hold him to a professional standard of conduct.[265] This practice is increasingly common with trustees and other specially skilled fiduciaries.[266] Alternatively, the settlor may wish to hold the trust protector to the same standard of conduct that applies to trustees when he exercises powers that are normally reserved to a trustee. In such cases, the drafter should identify these powers in the trust instrument and indicate what standard of conduct will be applicable.

B. Provide for the Appointment, Removal, and Compensation of Trust Protectors

The trust instrument should provide some mechanism for the appointment, removal, and compensation of trust protectors. This is especially important if the trust is expected to last for a long time. Although the appointment, removal, and compensation process does not have a direct bearing on a trust protector's fiduciary duties, it may affect them indirectly. In most instances, the settlor will appoint the original trust protector in the deed of trust, if the trust is *inter vivos*, or by will, if the trust is testamentary. However, assuming that the trust protector is an individual, it may become necessary to appoint a successor if the original trust protector dies, becomes incapacitated or is removed for some reason. The trust instrument should provide a mechanism for appointing a successor trust protector.[267] If the trust is *inter vivos*, the settlor might retain that power. However, if the settlor is dead the power to appoint a successor trust protector should be vested in someone. Otherwise, the trustee or the beneficiaries will have to petition a court to appoint one.[268]

Allowing the trustee to appoint a successor trust protector is one option.[269] This approach might compromise the ability of the appointee to act independently of the trustee. A better alternative might be to vest this power in one or more beneficiaries.[270] However, this approach threatens to undermine the successor trust protector's duty of independence. Another approach is to empower the trustee

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[265] *See* Duncan & Sarafa, *supra* note 33, at 790-91.
[266] *Id.*
[267] Fox, *supra* note 264, at 957.
[268] Gregory T. Densen, *Trust Protectors: Powers, Capacity, and Selection*, 41 COLO. LAW. 63, 67 (Sept. 2012).
[269] *Id.*
[270] *Id.*

and some or all of the beneficiaries to fill a vacancy when it occurs.[271] Of course, the disadvantage of this approach is that it results in an unwieldy combination of participants. Finally, the trust instrument could authorize a disinterested third party to appoint a successor trust protector, but then it would have to provide for a mechanism to replace the appointer if he or she died or became disabled.

Some of these problems can be avoided if the settlor appoints a bank or other corporate financial institution to serve as trust protector. Unlike private individuals, corporate entities do not die or become disabled.[272] Of course, they are many reasons for the settlor to choose an individual as trust protector instead of a corporate entity. First, an institutional trust protector, like an institutional trustee, will insist on being compensated, thereby increasing the cost of administering the trust. Second, some of the activities that a trust protector is expected to carry out may require personal knowledge of the beneficiaries and their personalities and financial circumstances. In such cases, it would be better to choose a family member instead. On the other hand, a corporate entity might be more suitable if the trust protector's principal responsibility is to provide legal or financial advice to the trustee. However, if that were the case, it would probably be better to avoid appointing a trust protector and instead authorize the trustee to hire an attorney or financial advisor for this purpose.

Removal presents problems as well. As mentioned earlier, a court can remove a trust protector for breach of trust. However, judicial proceedings are expensive, especially if they are contested. As with the appointment process, there are no good methods for removing a trust protector. It would not be wise to vest this power in the trustee because that might impair the trust protector's independence. The same is possible if the power to remove is vested in one or more beneficiaries, particularly if the trust protector has the power to modify the distributive provisions of the trust. Of course, the settlor could retain the power to remove the trust protector, but that is not a long-term solution to the problem.

Another aspect of the power to remove is whether the trust protector should be subject to removal only for cause. Removal for cause should be limited to incompetence, incapacity, or serious breaches of trust. On the other hand, if someone is given absolute discretion to remove the trust protector (other than a sole beneficiary), there is a danger that the trust protector would not be able to exercise independent judgment and would become little more

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[271] *Id.*

[272] Langbein, *supra* note 48, at 639.

than an agent of the person who had the power of removal.

The issue of compensation is often overlooked. Obviously, an institutional or professional trust protector will insist on being compensated. It is also good practice to compensate individual trust protectors, even if they are friends or family members, at least on a per diem basis for their time and expenses. The question is who should negotiate compensation issues with the trust protector? It is obvious that the trust protector cannot unilaterally determine his compensation. That would constitute a conflict of interest and might even result in self-dealing. The parties would also have a conflict of interest if the trustee determined the trust protector's compensation, assuming that the trust protector exercised supervisory powers over the trustee. In theory, the trustee could approve a generous compensation package in return for the trust protector tacitly agreeing not to oppose the trustee's decisions.

It appears that the only persons without a conflict of interest would be the settlor and the trust beneficiaries. The settlor would be in a good position to determine the trust protector's compensation if he or she was still alive and willing to do so. The settlor might also devise some sort of compensation formula based on objective criteria, such as the size of the trust corpus or a percentage of the trust income. Another approach would be to allow the trustee to negotiate the trust protector's compensation subject to approval by the beneficiaries.

Another issue is reimbursement for reasonable expenses that a trust protector incurred in carrying out his duties. The trust instrument should provide for the payment of travel and related expenses, as well as the cost of obtaining expert legal, financial, or other professional advice where needed.[273]

C. Consider Whether to Include an Exculpatory Clause in the Trust Instrument

Exculpatory clauses in trusts are designed to relieve fiduciaries of liability for certain acts or failures to act that might otherwise be considered negligence or a breach of trust. They are widely used in such instruments for both amateur and professional fiduciaries.[274] Both the Restatement (Second) of Trusts section 222 and the UTC section 1008 provide that exculpatory clauses are generally enforceable.[275] However, both declare that such clauses are

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[273] *See generally* Duncan & Sarafa, *supra* note 33, at 792.

[274] Hill, *supra* note 44, at 834.

[275] RESTATEMENT (SECOND) OF TRUSTS § 222 (1959); UNIF. TRUST CODE § 1008 (2000) (amended 2010).

unenforceable if inserting such a clause into a trust instrument is itself a breach of fiduciary duty. Furthermore, both also state that exculpatory clauses are to be strictly construed and limit their effectiveness in cases of bad faith, intentional misconduct, or reckless indifference.

Although the Uniform Trust Code recognizes that exculpatory clauses are generally enforceable, it also sets forth a number of "mandatory rules" that cannot be waived by the settlor.[276] For example, section 105(b)(2) declares that "the duty of a trustee to act in good faith and in accordance with the terms and purposes of the trust" is a mandatory rule.[277] In addition, section 105(b)(3) states that "the requirement that a trust and its terms be for the benefit of its beneficiaries" cannot be waived.[278] Furthermore, section 1008 declares that:

> (a) A term of a trust relieving a trustee of liability for breach of trust is unenforceable to the extent that it: (1) relieves the trustee of liability for breach of trust committed in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries; or (2) was inserted as the result of an abuse by the trustee of a fiduciary or confidential relationship to the settlor.[279]
>
> (b) An exculpatory term drafted or caused to be drafted by the trustee is invalid as an abuse of a fiduciary or confidential relationship unless the trustee proves that the exculpatory term is fair under the circumstances and that its existence and contents were adequately communicated to the settlor.[280]

Presumably, these principles would also apply to trust protectors insofar as the exercise of a fiduciary power is concerned. The primary purpose of an exculpatory clause is to discourage lawsuits against the trust protector by providing almost complete immunity from liability. However, the drafter must be careful to make sure that the exculpatory clause is consistent with the standards of conduct that have been imposed on the trust protector elsewhere in the trust instrument.

V. CONCLUSION

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[276] UNIF. TRUST CODE § 105(b)(1)(4) (2000) (amended 2010).
[277] *Id.* § 105(b)(2).
[278] *Id.* § 105(b)(3).
[279] *Id.* § 1008(a).
[280] *Id.* § 1008(b).

Trust protectors are a relatively new addition to American trust law. Because of their extreme versatility, trust protectors can be used in a number of ways to assist in the administration of private trusts. Trust protectors are now recognized in most states, largely due to the widespread adoption of the Uniform Trust Code. Nevertheless, there is a considerable amount of uncertainty about the powers and duties of trust protectors. One of the most troublesome areas of uncertainty is whether or when trust protectors should be considered fiduciaries.

In this Article, I have attempted to identify the standards of conduct that should apply to trust protectors. American cases involving trust advisors and decisions from foreign jurisdictions involving trust protectors provide support for the notion that trust protectors should be considered fiduciaries, at least for some purposes. The Uniform Trust Code and statutes from a number of American states also provide that trust protectors are subject to some fiduciary duties. I have concluded that the weight of authority, foreign and domestic, suggests that trust protectors should be required to act in good faith, adhere to the terms of the trust instrument, and exercise their powers in the best interest of the trust beneficiaries. I would add an additional requirement that a trust protector exercise independent judgment in carrying out the functions of his office. These standards are particularly appropriate when the trust protector exercises discretionary powers. Finally, the trust instrument can also hold trust protectors to a higher standard, especially when the trust protector is providing services of a professional nature.

At the same time, if the settlor so desires, the trust instrument may designate some of the powers granted to the trust protector as personal and not fiduciary in nature and thereby exempt them from any fiduciary standard of conduct. The settlor can also modify the default standard of conduct by inserting an exculpatory clause in the trust instrument. The lesson to be learned from this is that while a great deal of uncertainty still exists about trust protectors and the standards of conduct to which they are subject, much of this uncertainty can be reduced by the insertion of appropriate provisions in the trust instrument.